



KATHLEEN CONNELL
Controller of the State of California

December 17, 1997

**To the Citizens, Governor, and Members
of the Legislature of the State of California:**

I am pleased to submit the State of California's *Comprehensive Annual Financial Report* (CAFR) for the year ended June 30, 1997. This report contains all the information needed to fully assess the State's fiscal condition.

As the State's Chief Financial Officer, I am encouraged by California's strong economic performance. Employment is up, businesses are growing, and prospects for the future are bright. Californians have reason to be optimistic as we enter the new millennium. To ensure this future becomes a reality, however, government must become more efficient and reduce its administrative spending. By doing so, we will be able to generate the resources needed for investment in such critical areas as education, law enforcement, infrastructure, and health care.

The State Controller's Office is an example of how government can work better at less cost. When I assumed office in 1995, I authorized an independent performance audit of the entire Controller's Office to identify opportunities for improved efficiency and service. As a result of implementing the audit's recommendations, the Controller's Office has achieved a 12% reduction in staffing and budget savings that have risen to \$7.7 million annually. Within five years after implementing the audit recommendations, my office will have achieved \$32 million in budget savings. I believe performance audits are a powerful tool for reforming the way government does business and that every state agency would benefit from adopting this approach.

Reforming the State's budget process is a top priority for me. I remain strongly committed to enactment of legislation to require state agencies to use zero-based budgeting. Under legislation I sponsored, which passed the Legislature unopposed, agencies would be forced to justify every tax dollar they request, rather than basing their proposed budget on the previous year's spending level. This would instill a greater sense of accountability to taxpayers and provide much-needed incentive for government agencies to control costs. Although this bill was vetoed, I will continue to work toward its ultimate enactment. I also will continue to press for adoption of a two-year budget cycle. Passage of a two-year budget cycle will instill fiscal discipline, allow local governments to plan their respective budgets, and create a spending plan that is proactive to the needs of the State.

Fundamental changes in government are necessary, I believe, in order to prepare California for the 21st century, changes based on the principles of fiscal discipline and accountability. Just as these principles guide the operations of the Controller's Office — from our reporting on state finances to our audits of state and local governmental entities, collection of overdue debts, and other vital functions — we must work together to ensure they guide government at every level.

This year's CAFR not only reflects my office's commitment to professionalism, it also represents a milestone for the State of California. Just two years ago, the Controller's Office brought a more complete approach to the annual report process, producing the State's first CAFR. Last year, our CAFR was awarded the prestigious Certificate of Achievement for Excellence in Financial Reporting by the Government Finance Officers Association, another first for the State.

As it was last year, this CAFR was prepared based on nationally recognized standards. It is presented in three sections: Introductory, Financial, and Statistical. The Introductory Section includes this letter of transmittal and my financial overview. The overview presents a summary of financial data that is useful in evaluating the fiscal condition of the State. The Financial Section includes the general purpose financial statements, notes to the financial statements, and the required supplementary information. The Financial Section also includes the combining fund and account group financial statements and schedules, which are presented for the purpose of additional analysis. The Statistical Section includes selected financial and demographic information, generally presented on a multi-year basis.

Responsibility for the accuracy of data, and the completeness and fairness of the presentation, including all disclosures, rests with the State. To the best of our knowledge and belief, the enclosed data are accurate in all material respects and are reported in a manner that fairly presents the financial position and operation of the various funds, account groups, and component units of the State.

This CAFR could not have been prepared without the generous assistance and cooperation of all state agencies. We wish to thank the State Auditor and his staff for their audit of the financial statements contained in this report. I also am extremely grateful to my staff for their hard work and professionalism.

Sincerely,

A handwritten signature in black ink, reading "Kathleen Connell". The signature is fluid and cursive, with the first name "Kathleen" and last name "Connell" clearly distinguishable.

KATHLEEN CONNELL
California State Controller